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BUDGET DEFICITS, CAPITAL FORMATION AND THE STATE-FEDERAL RELATIONSHIP UNDER THE FEDERAL SECURITIES LAWS

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The views expressed herein are those of Commissioner Marinaccio and do not necessarily represent those of the Commission, other Commissioners, or the staff.

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Good Morning. It is indeed a pleasure to be with the North American Securities Administrators Association. I would like to thank you for this opportunity to participate in the second annual SEC/NASAA Conference. The importance which is attached to this conference by both NASAA and the SEC is reflected in the large number of states represented here today and the level of SEC staff participation. On behalf of the SEC, I would like to say that the Commission is committed to further improving cooperation among the various state systems and the federal government in the area of securities regulation.

One would have to look hard to find a better textbook example of the meaning of federalism than the state-federal structure for preventing fraud and abuse in the purchase and sales of securities.

Capital formation is the yeast that provides the margin of growth in a free market economy that reduces unemployment, controls inflation, and allows domestic industry to compete in an internationalized economy.

It has been 50 years since the passage of the federal securities laws. The passage of those laws was a recognition that a modern complex economy necessitated a federal presence as well as a state regulatory apparatus to maintain the integrity of the formation of capital by the public sale of securities to investors. Thus, the Securities Act of 1933 provided for the registration of securities to be sold in a national market and the Securities Exchange Act of 1934 provided a framework for industry self-regulation to undergird secondary market trading in those securities and provided a structure for liquidity and market pricing.

But the national interest in securities markets was not peremptory. Federal law explicitly recognized the important role played by state securities regulators.

I would say that the securities laws recognize that state and federal interests are inextricably interwoven of necessity by the very nature of the capital formation process. There must be in a modern economy a national capital market

(indeed there is rapidly developing an international capital market, but that is the subject of another speech), but there can be no ignoring state interests in the process, simply because state securities administrators have a duty to investors located within their states to ensure that they are not defrauded.

The dual system of state-federal securities enforcement has served the nation well. But in a dynamic domestic and world economy we cannot rest on our laurels. We must adapt to change in a creative and imaginative way.

An important factor operating in the national economy is the federal budget deficit. Eliminating the deficit is a national challenge. In its own way this challenge is going to force us to look closely at the state-federal relationship for enforcing the securities laws.

I take it as a given that so far into the future that we can reasonably predict, federal agencies will have to operate under budgets that do not provide the generous increases that they have in the past.

The SEC will not be immune from this process, nor should it be. If the federal deficit is to be reduced, all federal agencies will have to do their part and make their contribution, the SEC included.

The SEC has shown that it can operate efficiently and it will have to do more. We have not yet exhausted the potential for more efficiently accomplishing our task with the assistance of computers. But perhaps more to the point here today, we have only begun to think about the proper allocation of responsibilities between the federal (SEC) presence and the state presence to say nothing about the proper role of self-regulatory organizations in the process of enforcement of the securities laws.

Together we must arrive at a mutually agreeable allocation of enforcement responsibilities. The SEC must concentrate its efforts on larger frauds operating across state lines, and must leave to state securities administrators locally oriented fraud and abuse.

I think it is fair to say that the states are at the cuting edge of enforcement efforts concerning sales practices. You have a presence in every substantial city in the country. Accordingly, your contacts with local investment communities are far greater than that of the SEC. You also can react more readily to local fraudulent schemes by virtue of your cease and desist powers.

State enforcement efforts against fraudulent tax shelter offerings and exotic securities schemes have been particularly effective. The SEC tends to focus its efforts on financial fraud by publicly-held companies, fraudulent public offerings, wide-scale broker-dealer abuses and inside information cases. Our mutual efforts serve to roughly complete the matrix of State-Federal securities enforcement. I also applaud your initiatives in resorting to multi-state task forces to pursue regional interstate enforcement matters.

I would say that state enforcement activities will have to move into such additional areas as fraudulent private placements and Regulation D offerings; individual financial planner violators; local blind pool offerings; and individual registered representative frauds such as churning. Briefings and discussion will be presented today concerning these areas. I sincerely hope that candid discussion will ensue, and that we will conclude this Conference with a meeting of the minds and some concrete proposals calculated to enhance the protection of public investors -- particularly in the instance of capital formation by small firms and business ventures.

If we seek to channel our energies in pursuit of those matters that we, respectively, do best, I believe that, notwithstanding our shrinking collective resources, our enforcement presence can be more efficient and wide-spread. All to the benefit of the investing public.

Budget constraints will increasingly force us, quite correctly, I believe, to analyze the Federal interest in a case before the SEC commits resources. This will necessitate state securities administrators shouldering a bigger part of the enfocement load than they have heretofore. But that is how it should be. In the future we will not have the luxury of looking to the Federal level for solutions. In the process I have no doubt that as a general matter state personnel and budgets will have to be increased for securities enforcement and a continued commitment made to upgrading efficiency.

It is with respect to this last point that I wish to encourage the adoption of the Uniform Limited Offering Exemption (ULOE) in all of the 50 states.

In 1980, Congress enacted the Small Business Capital Formation Act (SBCFA) portion of the Small Business Investment Incentive Act. As respects small business capital formation the SBCFA updates the state-federal relationship regarding securities matters substantially from the framework in effect since the inception of the securities laws in the 1930s.

With the passage of the SBCFA, Congress recognized that the bulk of the jobs created in our economy are provided by small business and that uneven state-federal regulation can have a harmful effect on small business capital formation. Any such disincentives to small business capital formation under the securities laws caused by uneven regulation would decrease employment and our ability to compete against foreign competitors in the domestic and world economy.

The SBCFA authorized the SEC to cooperate with NASAA to assist in effectuating greater uniformity in state-federal securities matters.

Congress declared it to be the policy of the SBCFA to foster such state-federal cooperation to:

-- achieve maximum effectiveness of regulation;

-- achieve maximum uniformity of state-federal regulatory standards;

-- achieve minimum interference with the business of capital formation; and

-- substantially reduce costs and paperwork to diminish the burdens of raising investment capital and the costs of administering the securities laws.

It is clear from the plain language of the SBCFA that Congress meant to establish a new national securities policy toward capital formation for small business. The new policy was to be characterized by uniformity in state-federal regulation and a reduction in the cost and burdens of regulation. In order to develop a way of accomplishing the goals of the SBCFA, Congress mandated that the SEC is to conduct an annual conference.

The serious question for this Conference is whether we have lived up to the Congressional mandate. Under the dual system of federal-state securities regulation which has existed since the adoption of the Securities Act of 1933, issuers wishing to sell securities must comply with all appropriate federal securities laws as well as the regulations of each state in which they wish to offer and sell securities. The burden of complying with all such laws can be onerous, particularly for small issuers and tends to inhibit small business capital formation. Until recently, federal and state regulators have worked together informally on an ad hoc basis and with the American Bar Association but little in the way of relieving the burden on issuers has been achieved.

The initial SEC/NASAA Conference was held in Williamsburg in September, 1983. It presented the first opportunity for many state securities administrators to meet face to face with a broad-based segment of senior SEC officials and provided a forum in which all present could air their views. The issues covered were far-reaching and included the ULOE, uniformity in merit regulation by states which so regulate, and uniform registration forms for investment advisors and broker-dealers. In addition, committees were established and individuals were designated to coordinate, on a continuing basis, issues in the areas of corporation finance, enforcement, investment management and market regulation.

Since 1983, great strides have been taken toward increasing and strengthening the system of cooperation between federal and state securities regulators. The designated Commission representatives and their staffs have worked with members of the various NASAA committees on rulemaking and other projects on an on-going basis. Several examples come to mind, some of which will be discussed during the next day and one/half. First, staff members from the Division of Corporation Finance have met several times with NASAA's Small Business Finance Committee in an effort to revise and simplify Form D of Regulation D. This same coordinating committee established a procedure whereby Commission Regulation D interpretive letters are commented on and reviewed by NASAA representatives to help develop interpretations that will be uniform on both federal and state levels. Secondly, in September, 1984, NASAA announced its intent to join the SEC's efforts to implement an electronic disclosure system. Three states, Georgia, Wisconsin, and California, have been selected by NASAA to participate in a pilot project whereby Electronic Data Gathering, Analysis and Retrieval (EDGAR) filings would be made available to the states. Since April, 1984, the Division of Investment Management has established a training program for the state examiners in states with adviser examination programs and has already provided classroom and field training to Oklahoma, New Mexico and Florida state personnel. As a result of the 1983 SEC/NASAA conference, a NASAA committee was established to addresss the problem of unnecessary lack of uniformity in investment company regulation. Committee recommendations have already been made to the states to repeal expense limitations, and to adopt more uniform procedures for filing registrations, sales reports and advertising.

In the area of broker-dealer regulation, an extensive effort by NASAA and the SEC, in cooperation with the self-regulatory organizations, has resulted in the adoption by the Commission of a revised Form B/D for use by the Commission and the states. Finally, the Central Registration Depository ("CRD") which already provides a centralized computer system to process filings by securities salespersons, is well underway to being expanded to handle broker-dealer registrations as well.

In addition to cooperation in formal rulemaking projects, SEC staff meet frequently and attend and participate in major NASAA conferences and small NASAA committee meetings. The Commission's Division of Enforcement readily communicates with state counterparts with respect to individual cases and regional Commission staff meet on at least an annual basis with NASAA representatives in connection with jointly sponsored regional securities conferences. Representatives of NASAA also have been represented each year on the Executive Commttee for the SEC Government-Business Forum on Small Business Capital Formation and have contributed greatly to the Forum's success.

Having stated the foregoing, I must, in all candor, state that maximum uniformity in regulatory standards and the relief of burdensome and costly regulation under SBCFA has not yet been achieved. The existence of a dual standard of compliance and the cost of such compliance still interfere with the business of capital formation. I believe the economy is paying a price for this in lost jobs and decreased competitiveness.

You have received copies of an agenda for this meeting which was drafted cooperatively by the SEC and Richard Malmgren, Orestes Mihaly and Lewis Brothers on behalf of NASAA. Although all of the agenda items are of importance to the Commission, I would like to point out that the adoption by all 50 states of the ULOE, which provides for a uniform exemption from state registration, commands the highest priority. A revised form of ULOE, designed to coordinate with Regulation D and to be uniform among the states, was endorsed by NASAA on September 21, 1983, immediately following the last SEC/NASAA conference. Prior to that date, 20 states had adopted various exemptions only partially responsive to the provisions of Regulation D. As of today, approximately 30 states have adopted some form of ULOE. However, many of these 30 states have adopted versions of ULOE which vary significantly and often needlessly from one another. There-

fore, we are still a long way from uniformity. Expensive and time consuming reviews still must be undertaken in many multi-state private placements. Absent total acceptance of one ULOE by all the states, we will not reach our goal of minimum interference with the capital formation process. I strongly urge NASAA to continue its efforts to encourage every state to adopt, as expeditiously as possible, one ULOE to coordinate with Regulation D.

There are many important issues facing us today and a limited amount of time in which to discuss them. Let us spend this time identifying areas of duplicative regulation and determining what steps can be taken to eliminate non-productive duplication and unnecesssary regulation which inhibits capital formation and has adverse effects on unemployment and our ability to compete. Both the SEC and NASAA, must consider closely those areas in which the public would be better served by deference to the expertise of the other.